HOUSING MARKET OUTLOOK
Sherbrooke CMA

CANADA MORTGAGE AND HOUSING CORPORATION

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Highlights

- The resale market will remain favourable to buyers.
- Housing starts will reach lower levels than in the past.
- The vacancy rate will decrease slightly.
- Employment is expected to post a small increase.

Figure 1

Source: CMHC f: CMHC forecasts

The outlook is subject to uncertainty. Although point forecasts are presented in this publication, CMHC also presents risks where appropriate. The forecasts and historical data included in this document reflect information available as of October 16, 2013.

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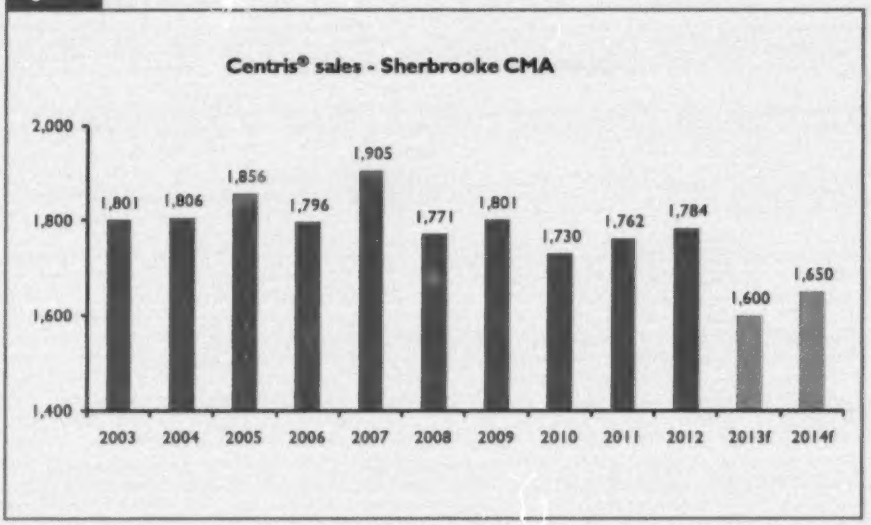
Existing home market: conditions softening

In the past few years, the resale market has been easing in the Sherbrooke census metropolitan area (CMA). This has been due to a decrease in sales (-9 per cent over 2012) and an increase in active listings (+6 per cent). In addition, the existing housing stock and the sustained pace of homebuilding recorded over the last five years have contributed to an increase in supply on the resale market and, as we will see in the next section, a rise in the stock of unabsorbed new homes. Less favourable economic conditions and a slowing job market also caused the market to ease. In the fall of 2012, the resale market shifted from being balanced to favouring buyers. The combination of these factors (increasing supply and decreasing demand) should keep the market favourable to buyers in 2013. In 2014, the market will start to stabilize. While remaining favourable to buyers, the market should stop easing thanks to more favourable economic conditions. The market could return to a balanced state in 2015, once the pool of buyers has replenished and the stock of unabsorbed new units has decreased.

Sales of existing homes should therefore drop by 10 per cent in 2013, to 1,600 units. In 2014, more favourable economic conditions will cause home resales to rise slightly, by 3 per cent, to 1,650 units. This should translate into a smaller increase in the average price, which should climb to $217,000 this year, up less than 1 per cent compared to 2012. In 2014, the rise will remain moderate, and the average price should reach $218,000.

By analyzing the market segments in greater detail, we see that the single-family home segment has been favourable to buyers since early 2013. This segment accounts for about 80 per cent of the sales in the area. While market conditions in this segment have eased, they remain close to being balanced. The condominium segment, for its part, has recorded a major slowdown since the beginning of the year. However, contrary to the single-family home segment, the condominium market strongly favours buyers, as sales decreased by 21 per cent year over year, while active listings grew by 17 per cent.

Figure 2



Source: QFREB by the Centris® system & CMHC forecasts

New home market: housing starts to reach lower levels than in past years

From January to September 2013, foundations were laid for close to 930 housing units in the Sherbrooke CMA. At this rate, we expect that total annual housing starts will attain 1,350 units at the end of 2013 in the Sherbrooke CMA, down 22 per cent from 2012. Better economic conditions will cause housing starts to rise in 2014, to 1,450 units, for an increase of 7 per cent over the same period in 2013. Despite this increase, the level of starts will remain relatively low compared to 2012, when close to 1,750 units got under way in the area.

The slowdown in activity on the new home market was caused both by the easing of the resale market, where the supply of homes for sale has been increasing, and by the rise in inventories of unabsorbed new units. In addition, the decline in employment in the area and less favourable economic conditions in the province overall were also factors that dampened the demand for new housing.

After showing renewed strength in 2012, single-detached housing starts will fall in 2013, to 450 units, for a decrease of 26 per cent year over year. The single-detached housing segment has been on the decline for the past few years; the growth in the construction of semi-detached and row houses—dwellings that are generally more affordable—caused a substitution effect among buyers.

As well, there is a will to promote intensification in the area. Finally, a possible increase in interest rates will make more expensive units less accessible, which means that the single-detached housing segment will continue to lose ground in the coming years. In 2014, thanks to the economic recovery, the volume of new single-detached homes should rise slightly, to 500 units, but will remain below the levels recorded in previous years.

In the multi-unit housing segment, the trends are mixed. Starts of semi-detached homes, a housing type that has grown in popularity over the past few years, will remain stable in 2013. However, row housing starts will fall by almost 75 per cent (see text box). Buyers now seem to be turning to condominiums. Finally, rental apartment starts should decrease in 2013, given the relatively high vacancy rates recorded in the area for the last few years.

The multi-unit housing segment should therefore post a decrease in activity in 2013 and then a slight increase in 2014. In fact, apartment and condominium starts should rise somewhat, but construction should stabilize in the other multi-unit housing categories.

Rental market: conditions easing

Rental housing starts have remained stable for the past few years, even if the rental market has eased. Several factors have supported this easing. Sherbrooke has recorded a strong movement to homeownership, which was fuelled by low interest rates and the increasing availability of affordable dwellings, such as condominiums and semi-detached and row homes. Also, the City of Sherbrooke's intention to provide some 100 social housing units annually may have contributed to the easing of the rental market.

Figure 3

Source: CMHC f: CMHC forecasts

In 2013, rental apartment starts will remain at the same level as in 2012. In fact, despite the high vacancy rate, demand is greater for newer rental units than for older ones. In 2014, rental apartment construction should start to decrease slightly.

Demand on the rental market should rise somewhat in the next few years. The strong movement to homeownership should ease off on account of the economic conditions. In addition, the Sherbrooke area shows positive net migration. A large portion of newcomers will turn to the rental market. The positive net migration among young people aged from 15 to 24 also pushed up demand for rental units: Sherbrooke is a university hub with eight institutions attended by some 40,000 students. This year, enrolment reached a record level at Bishop's University. In 2013, employment in the group aged from 15 to 24 has increased, which may have had a positive effect on the demand for rental units.

The combination of these factors (stabilizing supply and increasing demand in 2014) will cause the vacancy rate to stabilize in 2013 and reach 5 per cent. In 2014, the rate will decrease slightly to 4.8 per cent.

Economic trends: slowdown in employment and positive net migration

The Sherbrooke area has seen several fluctuations in employment over the past few years. After regaining all the jobs lost during the recession, the area has shown an overall downward trend in employment since 2012.

The service sector accounts for more than 50 per cent of jobs in the Sherbrooke CMA. Since the beginning of the year, the number of jobs in this sector has been decreasing. Also, the Institut de la statistique du Québec forecasts a 1.8-per-cent drop in investments in this sector by the end of 2013, which will have a negative impact on the employment level.

In addition, these job losses will be mainly felt among people aged from

25 to 44, a group that affects demand for homeowner housing. Employment among those aged from 15 to 24, for its part, has increased steadily since the beginning of the year. This group mainly influences demand for rental housing.

In 2013, it is estimated that the Sherbrooke metropolitan area will lose around 2 per cent of its jobs compared to 2012, with the level reaching 96,000 jobs. This will contribute to moderating demand on the housing market. The improvement in the Quebec economic conditions expected for 2014 should have a positive effect on employment in the Sherbrooke area, which should rise by 1 per cent.

In 2013, average weekly earnings have increased at a rate greater than inflation. The net result is positive real wage growth, which could have a positive impact on demand for homeowner housing.

In terms of net migration, more than 50,000 immigrants could settle in the province of Quebec in 2013, which will definitely have a positive impact on net migration in the Sherbrooke area, given that the CMA receives around 2 per cent of these immigrants each year. In 2012, net migration in the Sherbrooke CMA was positive, reaching 2,551 people, up by 3 per cent year over year.

Interprovincial net migration in the Sherbrooke CMA has been positive for the past few years. In 2012, it reached 587 people. In addition, over the last two years, net migration for people from 30 to 39 years has been positive. Therefore, the area would appear to be attracting more young families and young professionals, which could benefit the new home market, particularly in the more affordable market segments, such as semi-detached and row homes. Like every year, net migration for people from 15 to 24 years remained positive, thanks to the many colleges and universities in the area.

However, job losses could incite some people to choose an area where employment is stronger than in Sherbrooke. In this regard, we estimate that net migration will decrease slightly in 2013, to 2,450 people. In 2014, thanks to the anticipated renewed economic growth, net migration will increase to 2,550 people.

Mortgage rates to see modest and gradual increases late in the forecast horizon but will remain low by historical standards

Following the June meeting of the Federal Open Market Committee (FOMC) of the U.S. Federal Reserve Board, interest rates rose modestly and then remained steady in both the U.S. and Canada. According to the Federal Reserve Bank of New York, this reflected a change in the risk assessment of investors and not a change in the expected future path of interest rates.[1]

CMHC's interest rate forecast mirrors this view. Hence, mortgage rates have been slightly revised up in the third quarter of 2013 but, thereafter, follow the same interest rate path as before. Nevertheless, this interest rate outlook will continue to be supportive of housing market activity over the forecast horizon, as mortgage rates will remain low by historical standards.

Mortgage rates are expected to increase gradually and steadily over the forecast horizon. By the end of 2014, mortgage rates are forecast to be somewhat higher than in the third quarter of 2013. According to CMHC's base case scenario for 2013, the average for the one-year posted mortgage rate is forecast to be within 3.00 per cent to 3.50 per cent, while the average for the five-year posted mortgage rate is anticipated to be within 5.00 per cent to 5.50 per cent. For 2014, the average for the one-year posted mortgage rate is expected to rise and be in the 3.25 per cent to 3.75 per cent range, while the average for the five-year posted mortgage rate is forecast to be within 5.25 per cent to 6.00 per cent.

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1 "Preparing for Takeoff? Professional Forecasters and the June 2013 FOMC Meeting." Federal Reserve Bank of New York (2013). Richard Crump, Stefano Eusepi, and Emanuel Moench (http://libertystreeteconomics.newyorkfed.org/2013/09/preparing-for-takeoff-professional-forecasters-and-the-june-2013-fomc-meeting.html)

Spotlight on...

Semi-detached and row housing segment

In the past few years, the semi-detached and row housing segment has posted a boom in the Sherbrooke metropolitan area. Many developers were promoting the exceptionally low interest rates to tenants and were extolling the fact that a monthly mortgage payment was equal to a monthly rent. Many first-time buyers consequently made the move from renting to owning. The Sherbrooke area therefore experienced a strong movement to homeownership, which contributed to the increase in the vacancy rate in the CMA.

Since the beginning of the year, even if the semi-detached housing segment has continued to do well, row housing starts have seen a significant decrease, which can be explained by several factors. On the resale market, the single-family housing segment became favourable to buyers at the beginning of the year. Buyers therefore have greater choice in this market. Also, the stock of new units is trending upward, which means more selection for buyers.

On the demand side, first-time buyers often turn to the semi-detached and row housing segment, as this segment is the least expensive. The recent increase in interest rates and the decrease in employment in the area may have had a direct impact on demand for such homes.

Figure 4

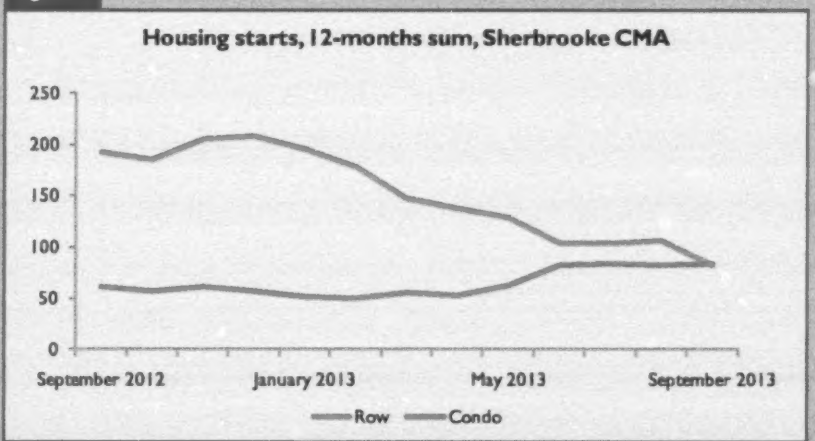
Source: CMHC

At the same time, while the condominium market remains favourable to buyers, there appears to have been a slight increase in condominium starts in the past few months, which indicates a certain shift in demand (probably on the part of first-time buyers) from the row housing segment to the condominium segment (see graph 5).

A share of potential first-time buyers could well decide to remain in the rental market, therefore limiting the increase in the vacancy rate in the Sherbrooke metropolitan area for the year to come.

In 2014, row housing starts are expected to stabilize and reach a lower level than in previous years.

Figure 5



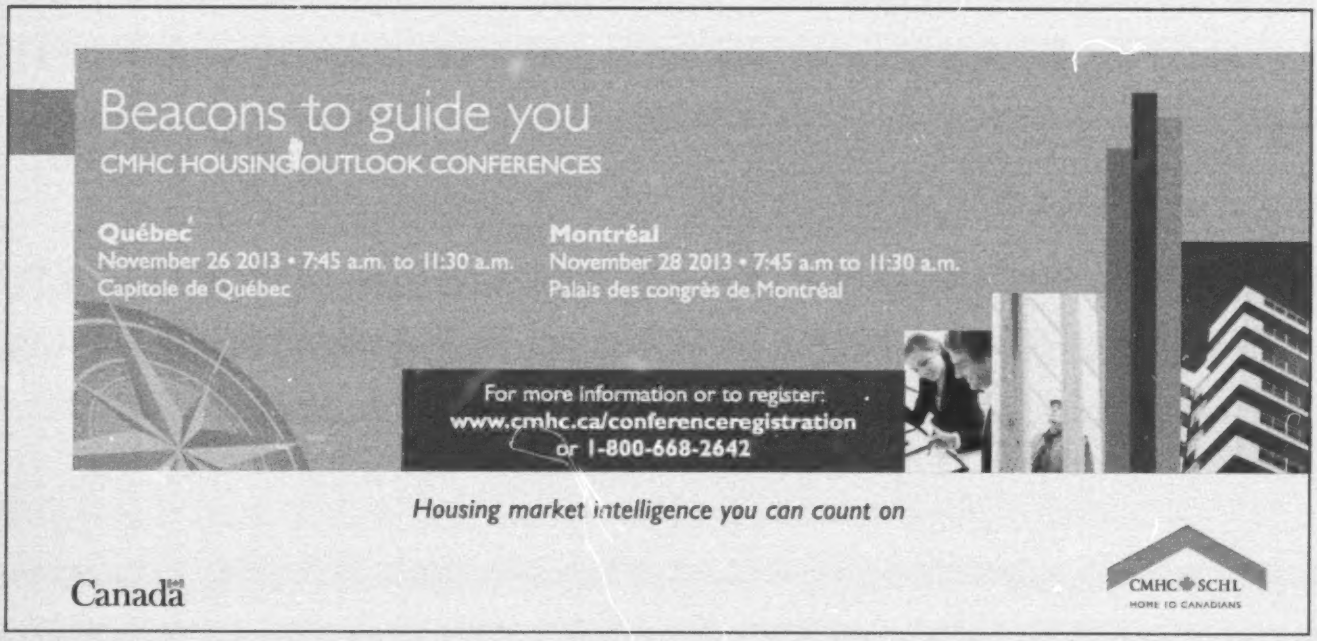
Source: CMHC

Trends at a glance

Key Factors and their Effects on Housing Starts	
Mortgage Rates	Mortgage rates will remain low by historical standards and supportive of housing demand.
Employment	After decreasing by 2 per cent in 2013, employment should grow slightly in 2014, which would sustain housing demand.
Income	In 2013, average weekly earnings have increased at a rate greater than inflation. The net result is positive real wage growth, which could have a positive impact on demand for homeowner housing.
Population	Positive net migration will stimulate demand for all types of housing in 2014, especially rental housing.
Resale Market	Conditions on the resale market will remain favourable to buyers in both 2013 and 2014, and prices will stabilize. The easing of the resale market will have a negative impact on the new home market.

Forecast risks

- The economic recovery expected in Quebec for 2014 will have a positive effect on the housing market.
- The expected increase in interest rates could moderate demand.
- The strength of the Canadian dollar continues to put the region at a disadvantage in regard to exports and tourism, which is moderating demand on the housing market.



Forecast Summary Sherbrooke CMA Fall 2013							
	2010	2011	2012	2013f	% chg	2014f	% chg
New Home Market							
Starts:							
Single-Detached	570	557	610	450	-26.2	500	11.1
Multiples	1,086	1,018	1,131	900	-20.4	950	5.6
Starts - Total	1,656	1,575	1,741	1,350	-22.5	1,450	7.4
Average Price ($) - excluding Magog:							
Single-Detached	197,101	184,319	220,353	221,000	0.3	223,000	0.9
Median Price ($):							
Single-Detached	170,000	170,000	180,000	183,000	1.7	185,000	1.1
New Housing Price Index (% chg) (Que.)	3.1	2.6	1.7	n.d.	-	n.d.	-
Resale Market							
Centris® Sales	1,838	1,883	1,784	1,600	-10.3	1,650	3.1
Centris® New Listings	3,544	3,630	3,578	3,500	-2.2	3,550	1.4
Centris® Active Listings	1,484	1,509	1,666	1,700	2.1	1,750	2.9
Centris® Average Price ($)	203,536	214,358	216,662	217,000	0.2	218,000	0.5
Rental Market - excluding Magog in 2006							
October Vacancy Rate (%)	4.6	4.7	5.0	5.0	-	4.8	-
Two-bedroom Average Rent (October) ($)	566	577	578	585	-	595	-
Economic Overview							
Mortgage Rate (1 year) (%)	3.49	3.52	3.17	3.00 - 3.50	-	3.25 - 3.75	-
Mortgage Rate (5 year) (%)	5.61	5.37	5.27	5.00 - 5.50	-	5.25 - 6.00	-
Annual Employment Level	92,600	99,000	98,100	96,000	-2.1	97,000	1.0
Employment Growth (%) - excluding Magog	-4.3	6.9	-0.9	-2.1	-	1.0	-
Unemployment rate (%)	7.6	6.9	7.5	7.8	-	7.5	-
Net Migration	1,816	2,477	2,551	2,450	-4.0	2,550	4.1

[1]The Centris® system contains all the listings of Québec real estate brokers.

[2]Source: CMHC (Starts and Completions Survey, Market Absorption Survey), adapted from Statistics Canada (CANSIM), Statistics Canada (CANSIM), Centris® Statistics. CMHC Forecast (2013-2014)

NOTE: Rental universe = Privately initiated rental apartment structures of three units and over

DEFINITIONS AND METHODOLOGY

New Home Market

Historical home starts numbers are collected through CMHC's monthly **Starts and Completions Survey**. Building permits are used to determine construction sites and visits confirm construction stages. A **start** is defined as the beginning of construction on a building, usually when the concrete has been poured for the whole of the structure's footing, or an equivalent stage where a basement will not be part of the structure.

Single-Detached Start:
The start of a building containing only one dwelling unit, which is completely separated on all sides from any other dwelling or structure.

Semi-Detached Start:
The start of each of the dwellings in a building containing two dwellings located side-by-side, adjoining no other structure and separated by a common or party wall extending from ground to roof.

Row (or Townhouse) Start:
Refers to the commencement of construction on a dwelling unit in a row of three or more attached dwellings separated by a common or party wall extending from ground to roof.

Apartment and other Starts:
Refers to the commencement of construction on all dwellings other than those described above, including structures commonly known as stacked townhouses, duplexes, triplexes, double duplexes and row duplexes.

Average and Median Single Detached Home Prices:
Are estimated using CMHC's **Market Absorption Survey**, which collects home prices at absorption and measures the rate at which units are sold or rented after they are completed. Dwellings are enumerated each month after a structure is completed until full absorption occurs. The term "**absorbed**" means that a housing unit is no longer on the market as it has been sold or rented.

New Home Price Indexes:
Changes in the New Home Price Indexes are estimated using annual averages of Statistics Canada's monthly values for New Housing Price Indexes (NHPI).

Resale Market

Historical resale market data in the summary tables of the Housing Market Outlook Reports refers to residential transactions through the Multiple Listings Services (MLS®) as reported by The Canadian Real Estate Association (CREA). In Quebec, this data is obtained by the Centris® listing system via the Quebec Federation of Real Estate Boards.

MLS® (Centris® in the province of Quebec) Sales:
Refers to the total number of sales made through the Multiple Listings Services in a particular year.

MLS® (Centris® in the province of Quebec) Average Price:
Refers to the average annual price of residential transactions through the Multiple Listings Services.

Rental Market

Rental Market vacancy rates and two bedroom rents information is from Canada Mortgage and Housing Corporation's (CMHC's) October Rental Market Survey (RMS). Conducted on a sample basis in all urban areas with populations of 10,000 and more, the RMS targets privately initiated structures with at least three rental units, which. have been on the market for at least three months. The survey obtains information from owners, managers, or building superintendents through a combination of telephone interviews and site visits.

Vacancy Rate:
The vacancy rate refers to the average vacancy rate of all apartment bedroom types. A unit is considered vacant if, at the time of the survey, it is physically unoccupied and available for immediate rental.

Two Bedroom Rent:
The rent refers to the average of the actual amount tenants pay for two bedroom apartment units. No adjustments are made for the inclusion or exclusion of amenities and services such as heat, hydro, parking, and hot water.

Economic Overview

Labour Force variables include the Annual Employment Level, Employment Growth, Unemployment Rate. Source: Statistics Canada's Labour Force Survey.

Net Migration:
Sum of net interprovincial (between provinces), net intra-provincial (within provinces), net international (immigration less emigration), returning Canadians and temporary (non-permanent) residents as provided to the CANSIM database by Statistics Canada's Demography Division. Sources of inter-provincial and intra-provincial migration data include a comparison of addresses from individual income tax returns for two consecutive years from Canada Revenue Agency (CRA) taxation records. The migration estimates are modelled, with the tax file results weighted to represent the whole population.

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